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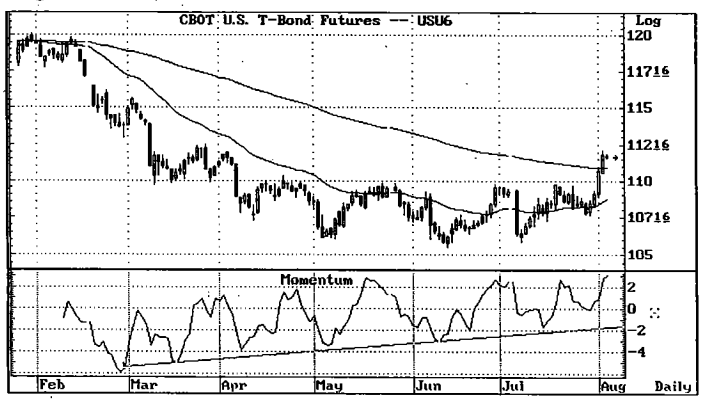
Aug. 14, 1996 **LETTER 1206**

THE PICTURE: The economic statistics have been pouring in, and the economists and analysts and experts and gurus are offering their predictions. In a recent *WSJ* piece, one "name" analyst predicted a one-thousand point rally in the Dow, while another equally well-known analyst predicted a one-thousand point Dow decline.

A bit of solid economic evidence came in on August 1 when it was announced that the Purchasing Managers' Index dropped from 54.9% to 50.2%. This news (which suggests a slowing economy) was immediately followed by a major upside breakout in the bonds (see chart) as the September bond futures, after completing a classic "rounding bottom" and a sensational rising momentum line, surged above their 110 resistance level.



Thus we have the old market paradox -- higher bond prices mean lower interest rates, but higher bonds prices also reflect a slowing economy -- and a slowing economy in turn could mean trouble for corporate profits. So much for the muddled and muddied economic background. Frankly, I have no strong opinions about the economy (that is, unless we get a Dow Theory bear signal).

THE MARKET: Actually (and happily), the stock market picture is moving towards ultimate clarification. This is why I can make that statement.

(1) It's now clear that the May-July stock market decline amounted to a full correction. Thus, the *lows for the various averages are now in place*, and those lows now become **critical "marker points,"** at least as far as students of Dow Theory are concerned.

(2) The critical lows are as follows: the D-J Industrials recorded a closing low of **5346.55** on July 23. The Transports recorded a closing low of **1965.73** on July 24. (Note: the large type for the lows is not a mistake, I placed those lows in large type because they are *so important.*)

(3) In the last Letter (page 6) I wrote that "the LONGER the Averages hold above the July lows, the MORE IMPORTANT those lows become." Believe it.

(4) The rally off the July lows in both duration and extent has gone far enough so that we can now call it a full upward correction of the preceding decline. And that's what makes the July lows so important.

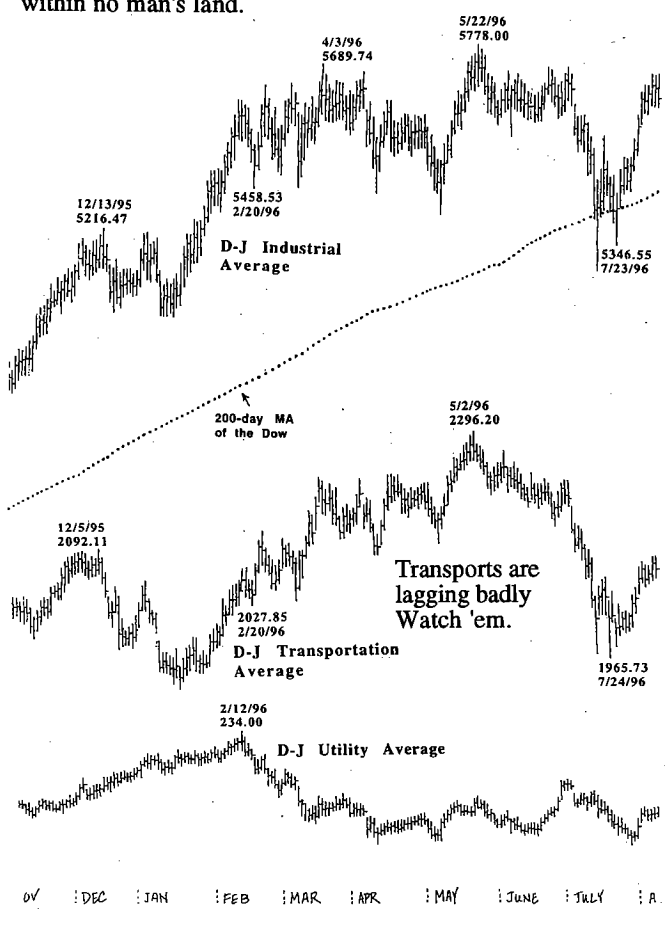
Aug. 2 DJIA 5679.83; PTI 4562; A-D Ratio -0.52
Aug. 9 DJIA 5681.31; PTI 4566; A-D Ratio -0.30
Dow Yield: 2.21%; Dow Price/Earnings: 18.0
Dow 200-day MA: 5405; Dow 30-day MA: 5544
Dow Times Book Value: 4.24; PTI 89-day MA: 4535
Percentage of Undervalued Blue-chips: 7%
Gold 200-day MA: 393.30; Gold-PTI: 483

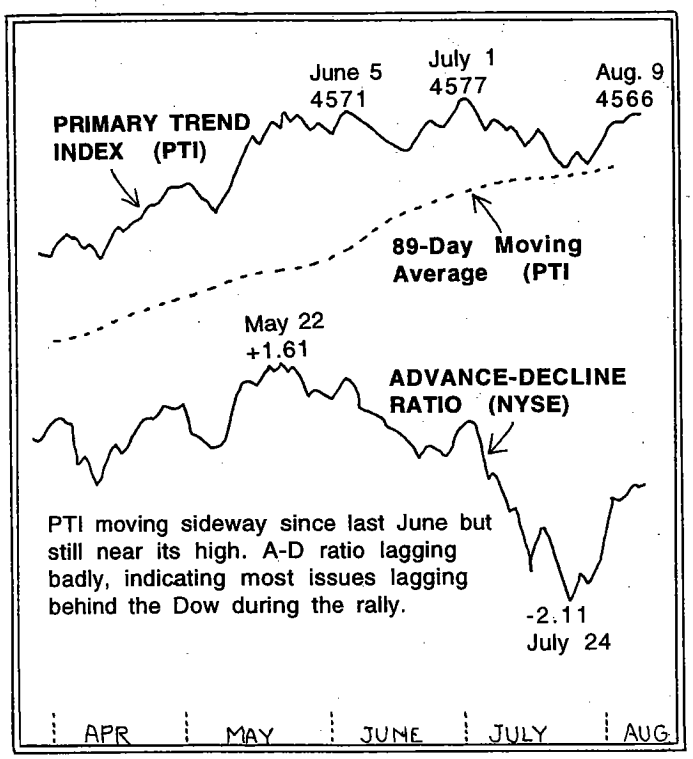
(5) The stock market is now in what I call "no man's land." We do not at this time know whether the ultimate resolution will be a further advance by BOTH Averages to new bull market highs. If this occurs, then obviously the bull market will be reconfirmed and even higher prices can be expected.

(6) However, if Industrials and Transports turn down and they BOTH break their July lows (increasing volume would add authority to any violation of the lows) -- then according to Dow Theory a primary bear market will have been signaled.

(7) At this point, the item that I note with particular interest is the sub-par recovery in the Transportation Average. The Transports have, as this is written, recovered only 26% of their May-to-July losses. The Industrials fared far better, having recouped 86% of their own May-to-July losses.

(8) Until the two Averages break out either to new highs or new lows, stocks will remain locked in that limbo that I call "no man's land." There is no more indecisive period, no more difficult situation to "figure out," than when the Averages are fluctuating within no man's land.





Question: Do you have any opinion as to which way the eventual breakout will come?

Answer: This is one of those times when I have the luxury of just sitting back and allowing the market to provide the answer. I say that because now that the correction lows are in place we finally have *definite numbers to watch on both the upside and downside.*

In deference to the bulls, we do have the old market standby which states that *"a trend once in force continues in force until proved otherwise."* At this point, we have received no "otherwise." So from this standpoint the "safe" bet is that the Averages will eventually return to, and break out above, the old highs.

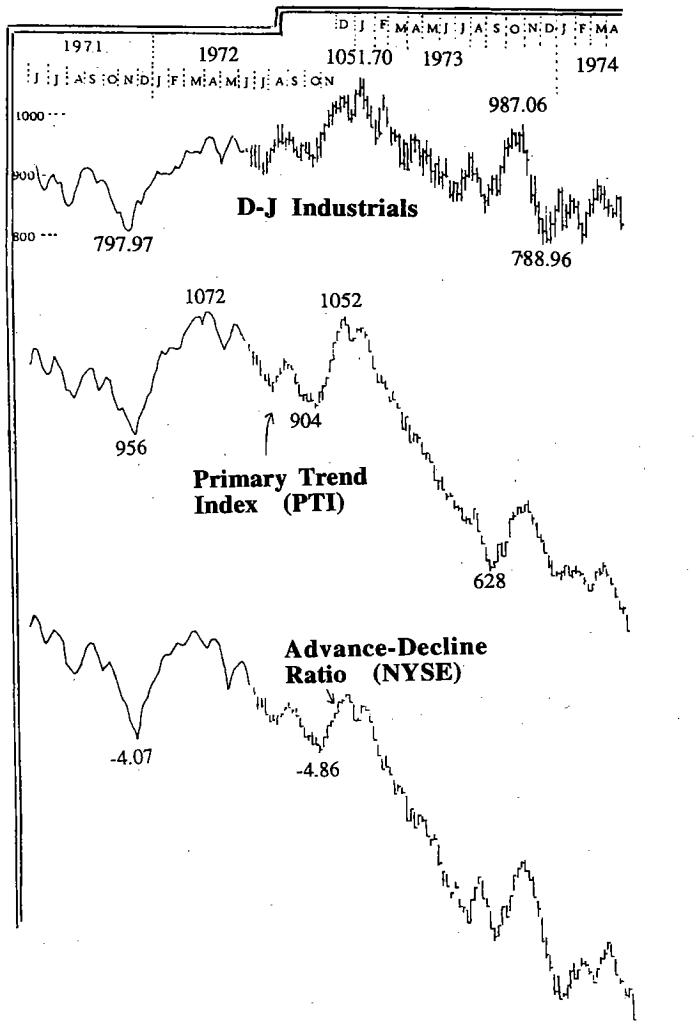
However, in the last Letter I advanced my own opinion that the stock market has made a top, and I continue to believe that is the case. If I am correct, then in due time both Averages will turn down and violate their July 23-24 lows.

BUT (there's always a "but," isn't there) let's turn to my **Primary Trend Index (PTI).** The PTI couldn't care less about the Russell opinion or anyone else's opinion. I noted in the last Letter that on the decline, the PTI did NOT break below its 89-day moving average. Furthermore, the PTI turned up on July 26, and it is now not far from its high. One thing I've learned over the years is never to fight the PTI.

CAN THE PTI DECLINE?: I've been getting calls from far and wide, most having to do with the Primary Trend Index (PTI) and its seeming reluctance to break below its 89-day moving average. Frankly, I've been surprised myself at the resistance of the PTI to decline. But 25 years of experience with this instrument convinces me that the PTI "knows what it's doing." And as I've said so many times in the past, "the PTI is a lot smarter than I am."

The recent decline in the PTI from a July 1 peak of 4577 to a July 24 low of 4534 represented a decline of only 43 points. Furthermore, on the decline the PTI refused to break below its 89-day moving average. What does this relatively minor decline mean? Is the PTI telling us that this market is considerably stronger than it appears on the surface? Answer: not necessarily.

I'm now being asked whether the PTI is even capable of heading down in a major way. In answer, I'm including a weekly chart reprinted from Letter 596 published back on **May 1, 1974.** Is the PTI capable of declining? You bet it is.



Here we see the initial peak in the PTI recorded in May 1972 at **1072.** A decline carried the PTI down to 904 in October '72, whereupon the PTI and the stock market embarked on a new rally. The rally took the Dow to a new all time high on January 11, 1973, but note that the PTI peaked at **1052,** 20 points *under* its previous high.

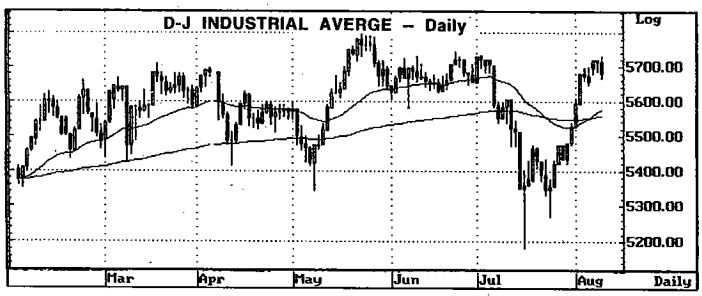
You want to know whether the PTI is capable of declining? Here's the answer -- from its January 1973 high of 1052, the PTI then **crashed 424 points** to a low of 628 in September 1973. A sharp rally ensued, followed by another swoon by the PTI to new lows. By December 1974 the Dow had collapsed to 577 with the PTI at an extreme low of **125.** That final plunge marked the bottom for both the Dow and the PTI. The long bear market had been brutal for most stocks, many of them having lost anywhere from 50% to 90% of their value. From its high of 1072 in 1972, the **PTI lost a huge total of 947 points.** So yes, the PTI is capable of declining.

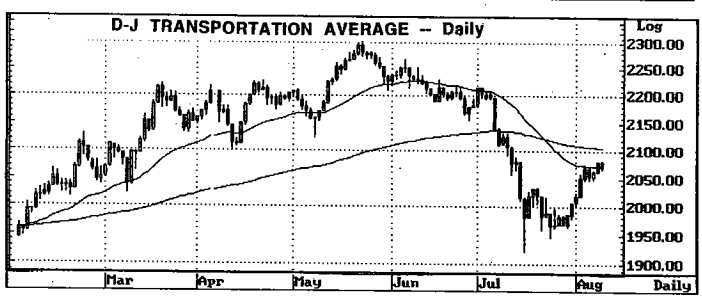
MOVING AVERAGE STUDIES: Continuing these studies from the last Letter, the explosive rally in the stock market resulted in the Dow and the S&P 500 surging above both their 34-day and 144-day moving averages. Furthermore, in both cases the 144-day MA turned up.

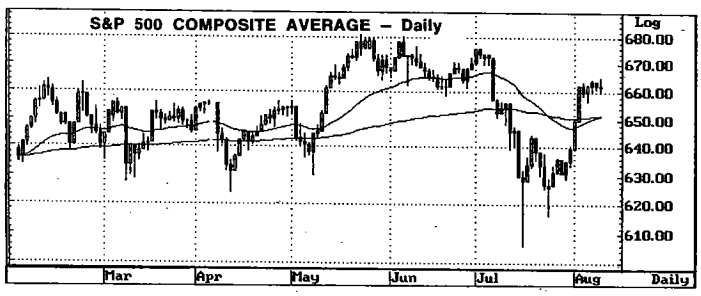
The Transports (by far the weakest of the four Averages) remain below both MAs -- although Utilities have now rallied above its own 34-day MA. On the other hand, the stronger Dow and S&P continue to hold above both MAs. As for Transports and Utilities, both are below their 144-day MAs and just as important, both of their 144-day (longer-term) MAs continue to decline.

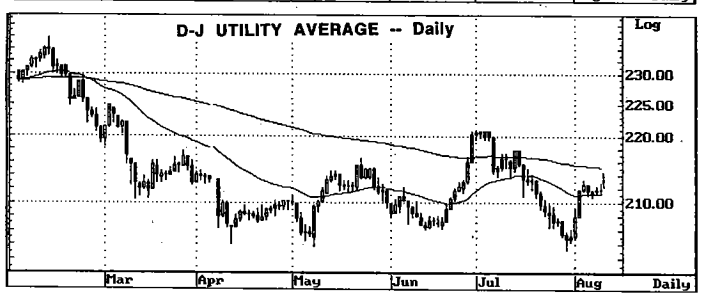
The position of the four items in relation to their respective MAs tells us clearly that strength resides in the Dow and the S&P while weakness remains in the Transports and the Utilities. From the

bullish standpoint, the lagging action of the Transportation Average and the advance-decline ratio remain the chief negatives in this market. Of course, the lack of new daily 52-week highs (NYSE) goes along with the lagging action of the A-D ratio, but it does constitute another negative in the total market picture.









INVESTMENT POSITION: The analysis on page 1 and 2 should suffice to explain why the question mark remains in this box.

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The fact is that the broad market (i.e., the majority of stocks) has gone nowhere over the last six months. Despite the violent July-August recovery in the Dow, the Nasdaq, the D-J Transports, the D-J Utility Average and the advance-decline ratio are still well below their previous highs. And of course, a great many stocks have suffered substantial losses which have not been recouped.

Thus our policy of remaining on the sidelines has been, in the main, beneficial. I'm holding to that policy.

I note that one name economist is predicting that business will continue to expand and that rates on the long bond will rise to 8%. If that happens, bonds will be in an important buying range. Remember that old Chinese adage, "All comes to he who waits?"

Question: do stock yields still have any meaning? One of the very few original thinkers in this business is Paul Macrae Montgomery of Legg Mason Wood Walker, Inc. In his latest bulletin Paul writes that "the notion that the 'average' return (on common stocks) is 10 1/2% is a highly misleading one. In the first place, of course, the indexes used in these studies include only the survivors, a fact which gives them an upward bias as compared to actual investor experience. The other problem is that it all depends on your starting point."

Paul then presents statistics compiled by Ned Davis Research which are a revelation. The statistics show five instances in which the Dow yield was at 2.96% or less along with 10-year and 20-year annual returns starting at those low-yield dates. The results are shown below and remember, the yield on the Dow as this is written is **2.28%**, even lower than the yields used in this study!

Date	Dow Yield	10-Year Annual Return	20-Year Annual Return
01/31/29	2.91%	-1.7	2.9
02/29/36	2.99%	7.5	11.8
07/31/59	2.95%	7.6	6.4
12/31/65	2.95%	3.2	8.5
03/31/87	2.96%		
		Avg 4.2%	Avg 7.4%

LOST: On July 31 the Post Office lost a small packet of mail that was addressed to us. These were all Dow Theory Letters' postage-free return envelopes containing subscriptions and trials. So if you recently sent in a subscription renewal, please check your mailing label for the appropriate expiration date. Apologies -- please let us know if your renewal was among those "misplaced."

NOTES & QUOTES: The yield on the Dow is now **2.28%.** *Investment Quality Trends* here in La Jolla notes that if the Dow was to go to a 3% yield (historically, a Dow yield of 3% was considered "overvalued"), the Dow would be priced at 4313. A decline to the 4% yield (no bargain, historically) would take the Dow down to 3235, a 45% loss from the high. At 6% (where the bear market of 1974 ended) the Dow would sell at 2157.

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Bonds: The following is from the excellent *Liscio Report* [(201)509-2256]: "Any rally in bonds will probably not endure beyond the election. Why the election? First of all, if Clinton wins, which is a virtual lock, bond traders will start to fret that he will steer the country much farther to left in his lame duck term. Again, it doesn't matter that Clinton is the least liberal Democrat to run for office since John W. Davis in 1924. Wall Street sees Clinton as a pot-smoking, draft-dodging, skirt-chasing, left wing crank. Should the Democrats regain control of Congress, or even pick up enough seats, those fears will only escalate. And what do you get if Dole wins? A 15% tax cut, the end of budget discipline, and an avalanche of sell orders in bondland." **Russell comment:** Sounds right to me.

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Tacky: Did you enjoy the Olympics? If you watched it over TV, you may have been as frustrated as I was by the one-channel, non-live, sporadic coverage, by all the "fluff" human interest reports, and by the intense concentration on US athletes (even in cases where foreign athletes won the metals). I got so frustrated with NBC's endless parade of ads that I just taped each segment and then fast forwarded through those never-ending ads. Being an old track man (the dashes), I was particularly interested in the track and field events. They were partly-covered in a kind of strange, disjointed way. I did catch quite a few of the running events. A lot of the heats weren't covered, and finally in frustration I turned to one of our local Mexican TV stations and got what I considered better coverage there with a lot less nonsense. Finally, even the International Olympic Committee got fed up and stated that it will never again approve a privately financed Olympiad without at least a government guarantee of the financing. Public money would reduce the need to sell so many ads. Conclusion: Sydney, Australia (Olympics in the year 2000) promises to give us a better showing -- minus the extreme commercialization and almost embarrassing flag-

waving. In a sentence, I found almost everything about this Olympics tacky except the great athletes (and yeah, I'm sick of King Carl and his king-sized me-me ego).

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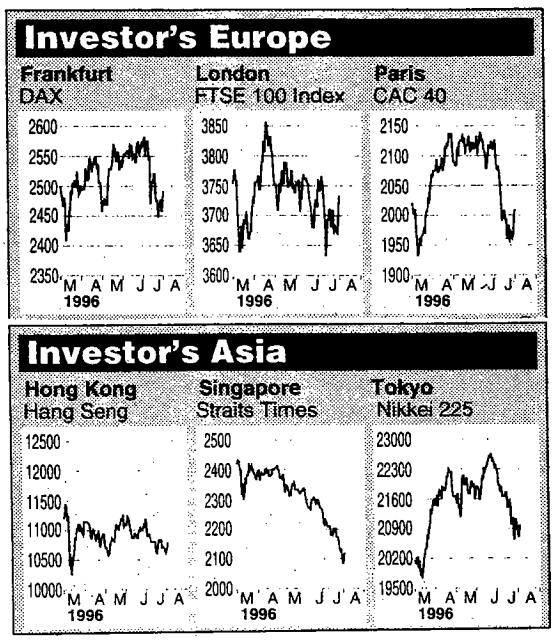
As Wall Street goes, so goes the world. That may not be absolutely true in a bull market (remember how the Nikkei outpaced the Dow for years following 1949), but on the downside, it's true. When the Dow runs into trouble, the rest of the world almost always follows. These charts from one of my favorite newspapers, the *International Herald Tribune* [(800) 882-2884] tell the story. Singapore's market weakness (from all accounts Singapore is booming economically) is particularly surprising. But markets look ahead. Question: If the US goes into a bear market, can you make money moving into other world markets, as so many gurus suggest? Answer: I doubt it; if the US goes into a big bear market, the whole world will almost surely follow.



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Trends: Sales of **women's apparel** in the US fell a whopping 12% from the record $84 billion in 1989 to the $73 billion of '95. Why? Women are dressing down to less expensive, more casual clothes. My wife, Faye, says she used to wear business suits to work five days a week, now she wears them two days a week (and that's to a law firm, and law firms tend to be ultra-conservative). **Music:** one of the hottest trends in radio is "smooth jazz" or "new adult contemporary." LA's FM station KTWV known as "the Wave" has seen its advertising rise 75% this year over last, as an increasing number of listeners tune in. I listen to our local "smooth jazz" FM station too -- and me an old hot jazz fan. The fact is that I'm sick of rock and roll, a bit tired of country and western, and I find the new smooth jazz something I can listen to all day. Sure it tends to be background music, but maybe that's what people want -- a little "peace" in a crazy world. **Films** reflect the psychology of the times. Fear, horror, violence, aliens, unknown menaces from outer space, that seems to be what's bringing crowds into the movie theaters. I think it fits into a strange sense of foreboding that has infected the American spirit. At the Olympics there was fear of an attack from outside. Security was omnipresent. At the San Diego Republican convention our mayor has announced that security will be the tightest ever at a convention with 18 government services watching over the San Diego event. Planes blowing up, a bomb at the Olympics, serial killers, drive-by shootings, out-of-control teenagers, hanky-panky at the White House -- can anyone or anything be trusted today?

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More Trends: In his latest report Martin Zweig (hello, Marty) offers an interesting study. Home sales now run at a pace of about 828,000 units a year or at a value of about $195 billion. "Over the nine years through 1990 (when bear markets and corrections were still allowed) New Home Sales ran about 9 times greater than mutual funds. In the first five years of the latest bull market, Home Sales totaled only about 51% more than Mutual Fund Sales as the later picked up steam." But get this -- over the first 5 months of 1996, net Mutual Fund Sales have boomed at an annualized pace of $247 billion, which is 27% greater than Home Sales. **Russell comment:** When home prices were rising year after year, people wanted homes. More recently mutual funds were where the increases were -- to the point where Americans were actually putting more money in funds than in homes. But in July -- whoops, fund buyers got scared and in July they put only $3.5 billion in mutual funds, lowest amount since November, '94.

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Wave of the Future?: One of the biggest factories on the California-Mexico border will be built and owned by an unusual partnership of S. Korea's giant Samsung, US-based Corning Glass and Japan's Asahi Optical. The factory will make specialty glass for computers, TV monitors and laser big screens. The new factory will employ up to 5,000 workers.

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For fiscal year 1996 the US government will spend about $1.7 trillion. State and local governments will spend about the same, bringing the total amount to nearly $3.5 trillion. This amounts to $50,000 for every family in the nation. I dunno, I don't feel I'm getting 50 grand worth of services or anything else from my government, my state or my city.

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Daily you hear some politician mouthing platitudes about "the rich." So c'mon, just who are the rich? According to the Census Bureau report, median household income for 1994 was $32,264, up slightly from an inflation adjusted $31,241 for '93 but actually below the '89 peak of $34,445. A recent mid-June Census Bureau report puts the **top 5%** of the nation's households at **$183,044.** At the same time, the average income of the top 20% was $105,945. So does an income of over $183,000 put you in the "rich column"? Maybe.

The IRS applies the *top tax rate* to single persons and married couples with taxable income of $256,500 and up. That's probably the best definition of who's rich and who isn't. Of course, $256,500 in NYC or San Francisco is a lot different than the same amount in Portland, Maine or Salt Lake City. But let me put it this way -- if you pull in $250,000 a year your government considers you RICH.

* *

Bob Dole chose ex-Buffalo Bills, ex-San Diego Chargers quarterback, supply-sider and liberal Jack Kemp for VP. Could be a shrewd move, since Kemp is closely associated with California. If the GOP can take California, Clinton would have a difficult time winning, although it would be possible. But the GOP most definitely NEEDS California. Get this -- the last time a Republican won the presidency without California was when James Garfield did it back in 1880! And in 1880 California had only 1.6% of the total electoral votes; today California has **10%** (54 out of 538). Dole has apparently decided to zero in on two items (a) lower taxes and later changing the tax system, and (b) character, which is aimed directly at slimeball Clinton. Thus Dole has finally come up with two items that Clinton can't copy.

I spent Saturday (Aug. 10) at an amazing party for the press sponsored by the Copley newspapers (no, I'm not a member of the press, I was invited to the party by my good friend, Judith Harris). The fantastic party was held outdoors, attended by over 6,000 media people and VIPs. The food and drink were incredible -- served by 32 major California restaurants including their chefs and owners (and yes, Wolfgang Puck of Spago and four of his restaurants were there and Wolfgang's sleeves were rolled up), plus over 40 wineries and breweries. I've never seen so many people so wide-eyed, and downing so much fabulous, gourmet food. A monster fireworks display started at 9PM triggering an unearthly scene and setting off about 50 car alarms. If the media doesn't have a good time in San Diego, it's not the Copleys' fault (I understand they spent over a million dollars on the party) and that didn't include the chow and spirits. Wot a party!

My old friend, Harry Browne, is the presidential candidate for the Libertarian Party. Harry correctly notes that Dole's 15% tax

reduction sounds a lot bigger than it actually is. The tax cut would bring the top rate down from 40% (where Clinton's huge tax boost put it) to 34%, which is still higher than President Reagan's 28% and higher than even President Bush's 31%.

In all honesty, you have to wonder what all the high taxes and all the big spending have done for this nation. In comparison with the way the country was prior to World War II, we now have high crime, high deficits, high debts, high taxes, high illegitimate birth rates, rampant drug use, deteriorating public schools, endless regulations -- and for what? You know something -- I may even vote for Browne.

* *

The statistics on Initial Public Offerings surprised me. California in 1996 raised money for a whopping 437 IPOs while the second biggest total in the nation came from Massachusetts, which produced a total of a mere 38. So it seems the real entrepreneurial money comes from the Coast. No wonder my wife, Faye, who's a corporate lawyer, has been so blasted busy.

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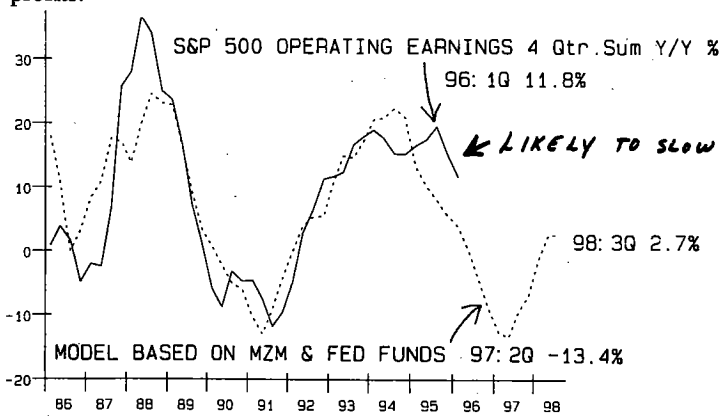
Is there any way to forecast corporate earnings (any way that works, that is)? One of the best ways may be a model (courtesy of Ed Hyman and *ISI*) based on the MZM (money of zero maturity) plus Fed Funds -- all moved two years ahead. This chart shows the model heading down into the first quarter of 1997, then turning up. If it works, corporate earnings will *head down* into the first quarter of '97, then turn back up. States Ed Hyman, Fed policy also leads profits by two years, suggesting that the Fed's last tightening move in early 1995 will have its maximum negative input on early 1997 profits.



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Political Comments Worth Repeating: "Strategy aside, the best reason for House Republicans to think they will keep their majorities is that Mr. Clinton felt compelled to sign their welfare bill despite his 20-point lead. It illustrates once again the ironic nature of his presidency, and especially of his re-election campaign: the Democrats may be leading in the polls but Republicans are winning the national argument. A Democratic president is being forced by the tide of history to repeal the Great Society he was supposed to re-energize. Mr. Clinton was elected as the last great liberal hope, but he's proving how conservative the nation has become" -- Gigot, in the Aug. 2 *WSJ*.

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Dem. Sen. Daniel Moynihan, in agony, on learning that the Welfare bill will pass (he was one of the first to warn of illegitimacy), "It (illegitimacy) has reached 50% -- half! In the Bronx it is 66.5%, in Manhattan 54%. Society has never dealt with this kind of thing. It has hit us like a cyclone, and in our confusion we are doing mad things. The premise of this legislature is that the behavior of certain adults can be changed by making the lives of their children as wretched as possible. This is a fearsome assumption." **Russell comment:** It's true, illegitimacy has run wild. This is one of the fruits of decades of liberalism and government welfare wherein people have forgotten how to take responsibility for their own lives. It's also a result of years of almost unchecked immigration plus the rise of the drug culture.

* *

From a fascinating *Forbes* interview with Lee Kuan Yew, Prime Minister of booming Singapore from 1959 to 1990: "We have brought the top tax rates down, down and down these past 30 years. Now 27% is our highest marginal rate. High taxes de-motivate people and are a burden that becomes increasingly onerous to bear. De-motivating people is most debilitating. You are taking away from a man a primeval urge. From Stone Age days he's had to hunt, get and keep meat for his wife and children. If you take that away and say, right, the government will care, then you've got a different society . . . How do you get people who have got used to this for 20 or 30 years to vote 'Yes, please take it away? Please, reduce it, in order that I will be competitive again and I will struggle to make my own living?' Newt Gingrich came in with the best of plans. But when it came to the crunch, President Clinton won. He came out on a white horse with shining white armor, to defend all the poor, the incapable, the infirm and the lame and the sick."

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Last week I received an interesting letter from A. G., a Hong Kong subscriber. He writes, "I worked and traveled around the globe last year to see the future and set my course after Hong Kong reverses to China in '97. I found that **(a)** Growth -- Europe and N. American renovates and repairs their industries and cities while Asia rebuilds. **(b)** Growth incentive -- the socialist systems in place in Europe are much worse than those in the US, and that both areas are debilitating their industry and their economic juices while Asia is entering the heroic stage of its growth. (Hong Kong personal tax returns are simple 1-page, 2-sided forms, with a tax rate of around 16% over a certain level of income.) **(c)** Security -- the US, Japan, Singapore, Hong Kong and Australia are, in general, SAFE places to live. **(d)** Life Style -- that only in the US. Singapore, and Australia can one have a comfortable (lazy?) life style. **(e)** Interesting Life/People -- it ain't in the US. It's in Asia; in the cities where one meets a confluence of the modern-day world's explorers of life and business. Every place else . . . boring people." **Russell comment:** Interesting and probably valid observations. But as for "e" -- c'mon, there are a few interesting people hiding in the US. You're probably disillusioned after watching too much of Howard Stern and David Letterman on TV.

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A new book by Phillip Longman is drawing a lot of interest. The title is "The Return of Thrift, How the Coming Collapse of the Middle-Class Welfare State Will Awaken Values in America." Longman notes that Americans are waking up to the fact that the Social Security System is a Ponzi scheme that has been "saved" (to great political acclaim) from impending bankruptcy at least twice -- under Jimmy Carter in 1977 and under Ronald Reagan in 1983. But despite 15 rate increases since the early '60s (more than doubling the payroll tax) the system's own trustees now admit that SS will run out of money around the year 2025 -- just about the time today's 35-year olds will be ready to retire. But Longman says that's just the beginning -- the Medicare Fund, the veteran's benefit programs and the pension systems for civil service and military workers all have huge as yet unfinanced bills coming due in the not-too-distant future. So he warns that the public must prepare for an "imminent collapse of the middle-class welfare state" that will cost most Americans "no less than a way of life." Longman estimates that benefits to the "non-poor" have reached a level of around $2 billion a day. Long-term reliance on government benefits is corrupting both the indigent and the well-off as well." **Russell comment:** I've been saying this for years. Debt, deficits and government handouts, all compounding, are building the foundation for future-shock and the next major depression (this, as the US cuts back on benefits to stave off insolvency).

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Business Week (Aug. 5) contains an interesting article concerning corporate profits. Jeffrey Fotta, president of Boston's Ernst Institutional Research makes a living looking for turn-arounds or trouble in corporations. Fotta uses a technique called dual cash-flow analysis which compares the cash a company receives from operations with cash coming from its balance sheet. This, he says, often allows him to detect signs of deteriorating fundamentals well before traditional cash-flow analysts. Fotta's method is turning up a "surprising number of warning signs at companies that otherwise look healthy." Among unfavorable companies by Fotta's methods are GM, Merck, Nucor, United Technologies, Hewlett-Packard, IBM, Allied Signal, Alcoa. Among unfavorable industries are Autos, Paper, Semiconductors and Steel.

BROADENING TOP: The last time I saw a broadening top in the Dow (at least, one that appeared as obvious as this one) was back in 1957. That pattern formed in the summer, and it was followed by a vicious straight-line July-December collapse that I'll never forget.

Whether the current broadening is fated to follow the 1957 pattern remains to be seen. At any rate, a broadening formation implies uncertainty, a wide-ranging difference of opinion, wherein the Dow swings first one way, then the other -- each rally carrying above the preceding and each decline dropping below the preceding. There are five turning points, and on the fifth the price action may advance to the upper trendline or it may fall short, often to be followed by an important decline.

The upper trendline for this broadening formation comes in just below 6,000, while the bottom trendline is just under 5,200. The halfway level of the pattern is roughly 5,500. So I'd say this -- a Dow decline below 5,500 would be a first sign of trouble, a drop below 5,400 (below the recent closing low) would look bad, and a close below 5,200 would be ominously bearish.

GOLD reputedly is in a long-term battle between the central banks and the mines on one side (they are the sellers) and the big gold bullion dealers and the goldphiles on the other side (they are the buyers). The further story is that the central banks and the mining companies are selling gold options in an attempt to lock in the gold price in the 375 to 400 range. When gold is around 375, they are buyers. When gold is near 400 they are sellers. At any rate, that seems to be the background.

Meanwhile, the speculators and everyone else interested in gold wait to see whether gold will sink below 375 or break out above 400. Since volatility in gold is now so low, gold options are cheap, cheap. For instance, you can buy a June 1997 call option on gold (actually, they expire nine months from now) at $410 for a 420 call, $330 for a 430 call and $210 for a 440 call (each call is for 100 ounces of gold). That seems awfully cheap to me -- I know I wouldn't be a seller of gold calls at those prices. In other words, the sellers of gold calls are saying that they don't see any big upside move in gold between now and the next nine months. Sellers of gold calls have been right for a long time, will they be right again? One cynic said that selling gold calls is comparable to an annuity. We'll see.

As for gold, it's actually been creeping up. In fact (shocker) October gold (futures) has rallied above its 34-day moving average (although it's still below its 144-day moving average, which now stands at 399).

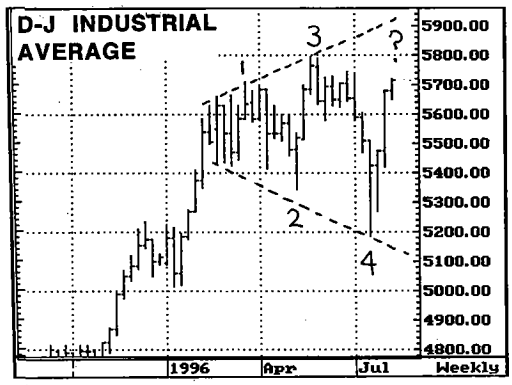
Turning to my Gold-Primary Trend Index (G-PTI), this Index has now formed the most "hopeful" structure since its March 26 high. The low was recorded on July 30 at 465. That low must hold.

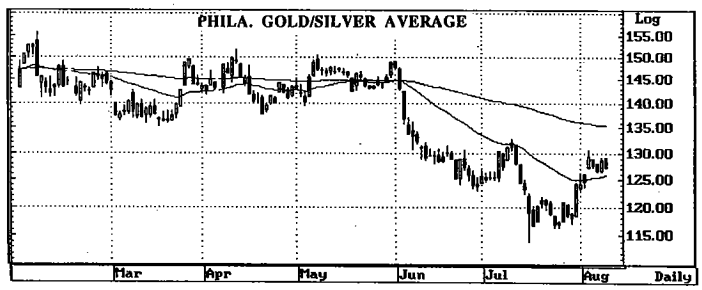
The Phila. Gold/Silver Average could be forming a head-and-shoulder bottom, and like gold it has rallied above its 34-day moving average but is still below its 144-day MA, which now stands at 135.

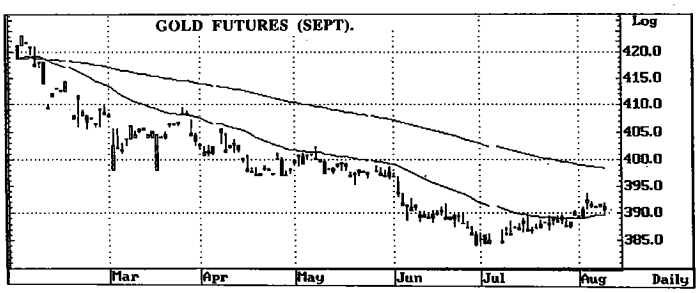
Barrick Gold is moving towards becoming the largest gold producer in the world. ABX is a very active explorer, with properties in every place from Nevada (its largest venture) to Chile to a projected takeover in Peru. ABX is acting better than the XAU Average, and anything above 29 1/2 would be impressive.

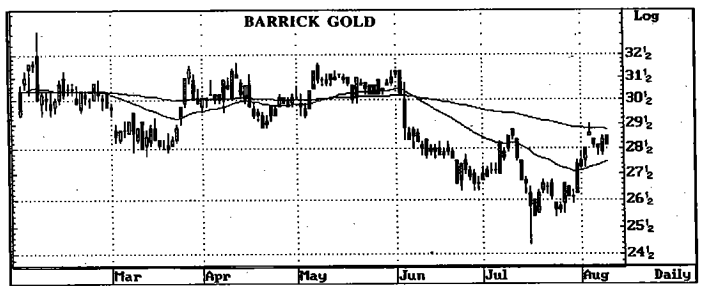
LATE NOTES: The Dow is the glamour-boy of this rally, having moved to within 60 points of its 5770.00 record high. So all eyes are focused on the Dow. However, I'm also watching the Transportation Average, and here the performance is a lot less impressive. Remember, a new Dow high (under Dow Theory) doesn't mean a thing unless it's confirmed by a new high in the Transports.

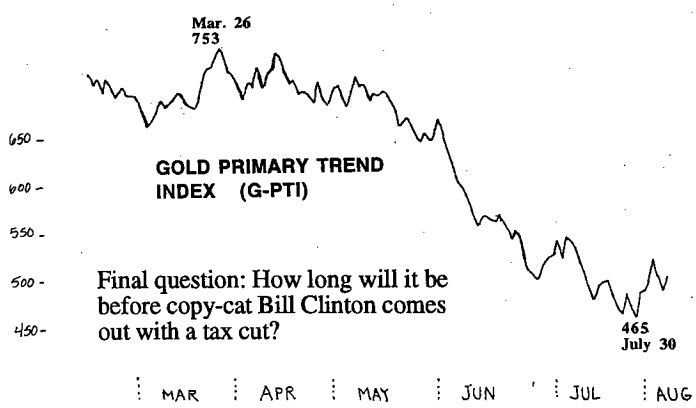
Many "experts" still deny the importance of the Transports as a confirming mechanism, and I think they're dead wrong. Forgetting the actual level of the Transports, the question is this -- if the Transportation Average hit a high in May (which it did), why can't it equal or better that high now? If it can't, then something is amiss in the transportation industry (i.e., airlines, trucks, rails). And since the Transportation Average reflects the sales and shipping capabilities of the nation, a sloughing off in the carriers tells us that something is wrong in the forthcoming business picture.











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